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ABSTRACT

The growth of cable television (CATV) will be limited unless present copyright practices are changed. The Federal Communication Commission opposes CATV's importation of distant signals because CATV is exempt from copyright liability. Now, almost all television programs are sold on the basis of long-term territorial exclusivity, which provides that the buyer has sole rights in his area to the program for a specified length of time. In most cases, cable cannot outbid the major broadcasters for programs. Thus there are four basic choices for cable policy: 1) abolish distant signal restrictions with no imposition of copyright liability; 2) abolish or restrict exclusives; 3) subject copyright owners to a compulsory license requirement, making their programs available for cable use at a regulated fee; and 4) impose full copyright liability and limit cable's market penetration. Of these, the second is most preferable. Exclusivity does not maximize copyright revenues. It is used mainly as a barrier against new stations entering the market for programs. Limiting exclusives benefits the growth of new stations and also benefits the public, who have a chance to see a program at more than one time slot. (JK)

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THE COPYRIGHT QUESTION IN CATV

by

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A Report Prepared for the
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The Copyright Question in CATV

Introduction

The question of CATV copyright liability for the importation of distant signals has, to date, been the most significant determinant of the fate of cable television. If Congress and the F.C.C., as well as the Supreme Court, accepted the principle of no copyright liability for cable carriage, then cable might well today be the major mode of television distribution. If, on the other hand, cable had been subjected to full copyright liability from the outset, then it might well have remained a minor, unthreatening adjunct to the broadcast industry. The current confused legal status and uncertain future prospects of cable television are traceable directly to the failure to resolve the copyright issue.

Some cable history, much of it already familiar to members of the Commission, is necessary to set the copyright question in context.

Cable Regulation and Copyright

At the outset cable was simply a reception service for mountain and rural communities which could not receive strong signals from nearby television stations. In these communities, cable served almost exclusively to supply a full complement of network service. While some communities may have been able to receive one or two networks before the advent of cable, the importation of the remaining network signals did not prompt

effective complaints by the stations which previously monopolized the market. Cable covered too small a population, and reception of three network signals had been too clearly established as a fundamental civil right, for protests to be availing.

Things changed in the late fifties and early sixties when cable began expanding into urban markets. In these territories, cable offered not simply clear network reception (often already available) but additional, independent channels whose signals were "imported" from nearby towns. These new signals represented additional, and highly potent, competition for the established network stations and, where they existed, local independents.

This new, urban growth of cable provoked intense pressure for federal regulation by the early nineteen sixties.[1] Since cable operators paid no royalties for the use of imported programs, program distributors objected that cable carriage of their programs amounted to use of their product without compensation. In addition, they argued that distant signal importation spoiled their chances for later sale of the imported program to a local station. Broadcasters, in turn, complained that competition from cable carriage of distant signals was unfair since cable systems "pirated" their programming without royalty payment while broadcasters paid in full. In particular, UHF broadcasters alleged

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1. See Hearings on S. Res. 224 and S. 376 Before the Senate Comm. on Interstate and Foreign Commerce, 85th Cong., 2d Sess., pt. 6 (1958); Hearings on S. 1939, S. 1741, S. 1801, S. 1886, and S. 2303 Before the Subcomm. on Communications of the Senate Comm. on Interstate and Foreign Commerce, 86th Cong., 1st Sess. (1959); Hearings on H.R. 7715 Before the Subcomm. on Communications and Power of the House Comm. on Interstate and Foreign Commerce, 89th Cong., 1st Sess. (1965); Hearings on H.R. 12914, H.R. 13286, and H.R. 14201 Before the House Comm. on Interstate and Foreign Commerce, 89th Cong., 1st Sess. (1966); H.R. Rep. No. 1635, 89th Cong., 2d Sess. (1966).

that cable carriage of distant signals would fractionate the audience for non-network programming and would add to the already formidable disabilities borne by UHF.

The F.C.C. proved responsive to all these complaints, especially those concerning the effect of distant signal importation on UHF.[2] Development of UHF has, since the early fifties, been the FCC's major hope for increased diversity in programming.[3] But even passage of the All-Channel Receiver Act, permitting the FCC to issues regulations requiring newly manufactured TV sets to carry UHF channels,[4] proved inadequate to assure the viability of UHF.

At the end of 1968, only twenty-five per cent of the available UHF channel allocations had been taken up, compared

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2. For development of FCC interest in this question, see In re Inquiry into the Impact of Community Antenna Systems, TV Translators, TV "Satellite" Stations, and TV "Repeaters" on the Orderly Development of Television Broadcasting, 26 F.C.C. 403 (1959); First Report; Second Report 770, 781; Notice of Proposed Rulemaking and Notice of Inquiry, 15 F.C.C. 2d 417 (1968); First Report and Order, 20 F.C.C. 2d 201 (1969). FCC jurisdiction over CATV was upheld in United States v. Southwestern Cable Co., 392 U.S. 157 (1968)

3. See Hearings on Regulation of Community Antenna Television Systems Before the Subcomm. on Communications and Power of the House Interstate and Foreign Commerce Comm., 91st Cong., 1st Sess. 8-30 (1969) (testimony of former FCC Chairman Rosel Hyde). As an additional indication of its paramount concern for UHF, the Commission has even prevented other broadcast stations (including sometimes other UHF's) from improving their broadcasting facilities because they would pose an economic threat to marginal UHF stations. See In re Selma Television, Inc., 12 F.C.C. 2d 781 (1968); Sarkes Tarzian, Inc., 8 F.C.C. 2d 342 (D.C. Cir. 1961). These and other cases are discussed in Brief for Association of Maximum Service Telecasters, Inc., MST comments on Part IV (Distant Signals), In re Amendment of Part 74, Subpart K of the Commission's Rules and Regulations Relative to Community Antenna Television Systems 41, FCC Docket No. 18397 (May 12, 1969.

4. 47 U.S.C. 303(s) (1964).

with eighty-four per cent of the UHF allocations. For a variety of technical and economic reasons, those UHF stations which have gone into operation remain mostly derivative in programming and anemic in financing. Faced with these disappointments, the FCC has chosen to ward off further (and, in its view, unfairly advantaged) competition from cable.[5]

At first, the FCC made no direct move against distant signal carriage. In its 1965 rules, the Commission merely required cable systems using microwave service to carry all local broadcast stations and avoid duplicating local programming with fifteen days before or after broadcast.[6] But in 1966, the Commission extended its jurisdiction to cover all CATV systems and prospectively forebade importation of distant signals into the country's 100 largest television markets (the "major markets," comprising eighty-nine percent of all television homes) without FCC hearing and determination that importation would be in the public interest, or waiver.[7] Major markets were singled out because it was there, the Commission reasoned, that UHF stood its best chance. In the three years during which these rules were operative, almost no waivers or favorabale determinations were granted for systems within the core of major markets.

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5. For the FCC's view on unfair competition, see United States v. Southwestern Cable Co., 392 U.S. 157, 175 (1968).

6. First Report and Order on Microwave-Served Community Antenna Television, 38 F.C.C. 683 (1965).

7. Second Report and Order on Community Antenna Television, 2 F.C.C. 2d 725 (1966).

Meanwhile, CATV development was further hampered when a copyright owner successfully prosecuted an infringement suit against cable carriage in the lower federal courts.[8] In 1968, however, the Supreme Court held that a cable operator did not "perform" copyrighted works and was therefore not liable for copyright infringement.[9] In quick response, the FCC adopted a new set of interim procedures which, while in some respects liberalizing its previous regulations,[19] amount to a reversal or sharp limitation

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8. United Artists Television, Inc. v. Fortnightly Corp., 255 F. Supp. 177 (S.D.N.Y. 1966), aff'd, 377 F. 2d 872 (2d Cir. 1967), rev'd, 392 U.S. 390 (1968).

9. Fortnightly Corp. v. United Artists Television, Inc. 392 U.S. 390 (1968). It has been suggested that the decision does not necessarily cover cable operators using microwave relay to import distant signals. See L. Johnson, supra note 1, at 18. This question is now in litigation. Columbia Broadcasting System v. Teleprompter Corp., No. 64-3814 (S.D.N.Y., filed Dec. 11, 1964). For a review of early stages of the copyright litigation, see Note, CATV and Copyright Liability, 80 Harv. Rev. 1515 (1967).

10. Previously, restrictive rules on distant signal importation within the 100 major markets had applied to CATV's operating within the "Grade A predicted Contour" (a measure of quality of television reception) of any station located in the market. Different stations' contours vary considerably in size, and some extend to sixty miles radii. In the 1968 proposed and interim rules, the Commission would restrict only CATV's operating in communities located in whole or in part within thirty-five miles of the main post office of the "designated community" of the major television market. FCC Notice of Proposed Rulemaking and Notice of Inquiry, 15 F.D.C. 2d 417 (1968). The "designated community" is the community which gives the major market its name, and may include more than one community in a given market. (E.g., market number thirty-eight in 1968 was Grand Rapids-Kalamazoo). For criticism of this new standard, see Note, The FCC's Proposed CATV Regulation, supra note 1, at 1708-10.

of the Supreme Court decision.[11] In form, the rules permit CATV outlets to import distant signals upon receiving a waiver from the FCC and "retransmission consent" from the distant broadcaster.[12] But, as the Commission soon made clear, such consent cannot amount to a mere quitclaim; the station has to have full authority to dispose of the copyright owner's interest in the program.[13] Since sales agreements between the copyright owner and the broadcaster generally do not grant such rights to the broadcaster, blanket retransmission consent would be virtually unobtainable.[14] Indeed, in the first two years of the new procedures' operation, waiver based on retransmission consent were requested by cable systems in only two or three cases.

In July 1970, the Commission proposed a major liberalization of its rules on cable television contingent upon Congressional

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11. The Commission clearly indicated its concern with redressing the unfair competitive advantage of cable. FCC Notice of Proposed Rulemaking and Notice of Inquiry, 15 F.C.C. 2d 417, 432-33 (1968). Former FCC Chairman Rosel Hyde, in testimony before a House subcommittee, virtually stated as much. See Hearings on Regulation of Community Antenna Television Systems, supra note 1, at 13, 25.

12. See FCC Notice of Proposed Rulemaking and Notice of Inquiry, 15 F.C.C. 2d 417 (1968).

13. FCC Order No. 18397, at 4 (Jan. 15, 1969)

14. L. Johnson, The Future of Cable Television: Some Problems of Federal Regulation (Rand Memorandum RM-6199-FF, 1970) p. 17.

solution of the copyright question.[15] Under the new rules, cable systems would be allowed to import up to four distant signals, subject to the requirement that they substitute for the advertising carried by the distant signal commercials sold on behalf of local UHF (and financially vulnerable VHF stations.) This plan is discussed further below.

While F.C.C. rules have effectively stopped the importation of distant signals, no explicit solution of the copyright question has yet emerged from Congress. Both cable operators and copyright owners predicted, in 1966 and 1967, that Supreme Court resolution of the copyright question would clear the way for a negotiated settlement. But the Court's Fortnightly decision merely shifted the arena to Congress. For several years passage of the omnibus copyright revision bill has been held up because of the CATV question. Pro-cable forces, represented most strongly on the Senate Judiciary Committee's copyright panel, and pro-broadcaster elements, lodged chiefly in the Senate Commerce Committee, have fought each other to a standoff. Attempts by cable and broadcast industry representatives to reach a negotiated settlement have been thwarted by threatened anti-trust action and, more

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15. See F.C.C. Second Further Notice of Proposed Rulemaking, In the Matter of Amendment of Part 74, Subpart K, of the Commission's Rules and Regulations Relative to Community Antenna Television Systems; and Inquiry Into the Development of Communications Technology and Services to Formulate Regulatory Policy and Rulemaking and/or Legislative Proposals. (Docket No. 18397) (July 1, 1970).

importantly, by each side's willingness to try its luck in the political arena.

The Current Situation

The situation, then, is as follows. Cable cannot grow (beyond a minor degree of expansion into remaining underserved areas and a few large cities with significant reception problems) because, without distant signals, it has little to offer. The only significant, avowed reason for regulatory opposition to distant signal importation is CATV's exemption from copyright liability. Yet no proposal for copyright payments has found any significant measure of acceptance.

At first glance, there would seem to be a simple solution to the dilemma. Why not subject cable operators to copyright liability, placing them on a par with broadcasters? If the programs shown on distant signals are so essential to their success, and if CATV serves as manifest a public need as its proponents claim, cable revenues would seem ample to support copyright payments. If they are not, then the market alone, not the F.C.C. or Congress, will be responsible for cable's failure.

Exclusivity

The difficulty with this argument lies in the marketing practices of programs owners. Almost all television programs are sold on the basis of long-term territorial exclusivity[16] -- that is, on contracts which provide that the program owner cannot

16. See N.Y. Times, Dec. 21, 1969, §3, at 8, col. 8. The prevalence of exclusives is recognized in First Report and Order on Microwave-Served Community Antenna Television, 38 F.C.C. 683, 703 (1965) (hereinafter cited as First Report) and Second Report and Order on Community Antenna Television, 2 F.C.C. 2d 725, 779-80 (1966) (hereinafter cited as Second Report).

license the same show to any television outlet (usual including cable systems) in the geographical area of the purchaser for a specified length of time, usually two to seven years.[17] The specified geographical area of exclusivity is subject to negotiation in individual deals, but is usually based on one of two standardized definitions of television broadcast coverage (Grade A and Grade B contours).

The importance of exclusivity is that it makes attractive programs virtually unavailable to all but the largest broadcasters in a market area. No one can afford to be the high bidder for exclusive rights unless the program is worth more to him than it is to any competitor. Thus, for example, suppose that a first-television-run showing of "Love Story" could command a 35 rating on any of the VHF stations in an area, a 20 rating on a UHF station (lower because of the technical inferiority of UHF transmission and the unwillingness of many viewers to attach the necessary UHF antenn or take the trouble to tune properly), and an audience on cable consisting of 80% of subscriber homes. Then a UHF station could afford to outbid a VHF station for exclusive rights only if (1) its 20 per cent of the total potential television audience would be worth more to advertisers (and hence to the station) than would 35 per cent on the VHF or (2) it were

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17. According to comments filed by a number of comm ercial and educational television stations in the FCC proceeding on territorial limitation of exclusives, "a large majority of feature film contracts appear to call for five to seven runs over a period of five to six years, while contracts for syndicated series only infrequently provide for more than two runs or extend beyond two years." Comments of WANE-TV, In re Amendment of Part 73 of the Commission's Rules with Respect to Television Programs Produced by Non-network Supplies and Not Made Available to Certain Television Stations 16-17, Docket No. 18, 179(1968).

willing to pay more because of the prestige it would acquire by running a smash movie. The cable system could afford to be the high bidder only if the extra subscriber revenues it could reap by offering "Love Story" exceeded the advertising value of the extra viewers which the movie would attract to a broadcast situation. But since an extra subscriber is worth approximately $60 a year to a cable system, while an extra viewer is worth approximately $45 a year to a broadcast station, the cable system could be the high bidder only if the extra number of subscribers it could attract by offering high quality shows would be roughly comparable in magnitude to the number of extra viewers a broadcast station could attract (at zero marginal cost to the viewers) by offering the same shows. For most programming, the broadcaster can attract far more free viewers than the cable owner could subscribers. Thus the high bidder under a system of exclusivity turns out to be the station with a large audience base.

A shift to full copyright liability would, then, subject cable to the necessity to bid for exclusive rights. Ordinarily it could not afford to purchase exclusivity for blockbusters, or even for most tolerable second and third run programming; it would end up with the warehouse epics which currently grace UHF schedules. But if cable could offer no more than this, it would have little more than it presently possesses to attract urban subscribers.

Thus there are four basic choices for cable policy: 1) abolish distant signal restrictions with no imposition of copyright

liability; 2) abolish or restrict exclusives; 3) subject copyright owners to a compulsory license requirement, making their programs available for cable use at a regulated fee; 4) impose full copyright liability, and limit cable's market penetration.

No Copyright Liability

The first of these alternatives would involve the most substantial change in the current structure of the television industry. If cable were free to import distant signals without copyright liability, program owners could sell their shows in one of two ways. They might choose to sell them first to a small broadcast station, whose advertising rates would reflect the fact that cable systems all over the country could pick up the program once it was broadcast. The show might also be sold for later transmission to other broadcast stations, which presumably would remain forbidden by law to carry the originating station's shows without permission. On the other hand, program owners might choose to sell the show to cable systems on a system-by-system basis, thereby excluding them from the right to pick up the show for nothing, and allowing the copyright owner to extract not merely a portion of total advertising sales (as he would under the first plan), but a fraction of cable subscriber revenues as well.

So long as cable represents only a small part of the total television market the first pattern of dealing might predominate. But cable should grow rapidly once it obtained unrestricted access to the complete stock of television programming

in the nation; and, after the number of cable subscribers reached a certain percentage, program owners would flock to the second mode of dealing. The result, eventually, would be the atrophy of broadcast TV as more and more of its shows found their way onto the cable.

This result seems undesirable for several reasons. First, it validates precisely the claims of pay-TV and cable-TV opponents that viewers would be forced to pay for what they now get "for free." Even though current programs aren't really free, their cost of production is built into the sales price of products, and thus affects viewers of different income groups in a manner which is more or less proportional to income. Subscriber TV, on the other hand, would be paid for on the basis of an equal per-set charge, with far more regressive incidence. Moreover, replacing the current investment in broadcast facilities with cable might prove to be an uneconomic use of resources. The substitution might simply expand program owners' revenues without resulting in much new programming. (This argument assumes, admittedly without much evidence, that the additional revenues would largely go to additional "rents" (i.e., scarcity wages) for television performers and other specialized resources.) If this were the case, the social cost of laying the cable may outweigh the social benefits of new program production.

A final, and most significant, objection to the proposed regime is its irrational discrimination between two technological modes -- cable and broadcast. There is no obvious reason why a show once broadcast should lose its copyright protection vis-a-vis

cable use, while one initially played on the cable is not similarly shorn. Nor is it clear why, if broadcasting divests the copyright with respect to cable pickup, it should not have the same effect for rebroadcasting on other television stations.

Limitations on Exclusives

It would seem, on first impression, that any limitation on exclusivity might threaten to erode the profitability of program ownership and thus inhibit program production. Exclusivity, one might assume, is used by copyright owners because it maximizes their profits. If exclusivity were curbed, copyright revenues would suffer and the aim of the copyright laws (increased production through legalized monopoly profits) would be frustrated.

The problem with this argument is its premise: exclusivity does not seem to maximize copyright revenues. There is no apparent reason why a single exclusive sale should produce higher profits than multiple sales on a non-exclusive basis. Elsewhere, Leonard Chazen and the author have enumerated the possible profit-maximizing reasons for exclusivity (such as reduction of transactions costs, creation of station prestige, and avoidance of scheduling irrationalities)[18] and argued that they would not outweigh the revenue-losing feature of exclusives (namely, that fewer people watch television, and thus there is a lower total amount of advertising revenue and program payments, when programs are sold on an exclusive basis.)

If exclusives are not clearly profit-maximizing, why are

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18. Chazen & Ross, "Federal Regulation of Cable Television: The Visible Hand," June, 1970 Harvard Law Review.

they used? The reason seems to be that they create a barrier to entry into broadcasting and networking. So long as exclusivity predominates, CATV's and UHF's are virtually precluded from the market for attractive programming. Copyright owners probably do not receive any direct compensation for their part in creating this barrier to entry. But since the broadcasters and networks with which copyright owners deal have substantial market power the copyright owners would need a strong profit motive to risk their olisopolistic customers' wrath by abandoning a practice which has advantages for the customers and no disadvantages for them. The Chazen-Ross article concludes that although exclusivity does not gain the copyright owners anything, it does not cost them much, either. Hence it persists because of inertia and broadcaster pressure.

Given this conclusion, it seems reasonable to resolve the copyright problem by limiting or abolishing exclusives. If there were no exclusives, programs would be sold on a per-thousand-audience basis: each broadcaster (or cable owner) would pay for a program in proportion to the amount of its attractiveness he used up by playing it on his station. Cable operators and UHF stations could then perfectly well afford to purchase the programs now being shown on VHF; these programs would be run, roughly simultaneously, on a number of stations at a number of times until their welcome was sufficiently well worn to require temporary retirement. The result would be greater consumer satisfaction (since having the same program available at different times ranks as a major reason for viewer interest in imported

distant signals), and increased abundance of television channels. The F.C.C. would no longer have to strike an administrative balance between cable and broadcast television, but could let market forces do their work. Cable systems would survive or falter depending on their ability to pay for programming on the same basis as broadcasters.

There are three possible regulatory strategies toward exclusives. First, exclusivity could be preserved but limited in duration to, for example, three months. Such a measure would insure that programming would eventually find its way to cable and UHF outlets, though perhaps only on the fourth or subsequent run. A second possibility would be to preserve exclusivity for the first run, but require sale on a per-thousand-audience basis for subsequent showings. Finally, exclusivity could be prohibited altogether, and all sales be required to be based on audience obtained. Some technical problems attend each of these measures though there is no reason to believe that the difficulties are substantial. The FCC's recent Notice of Inquiry into exclusives, extending the earlier inquiry into the geographical reach of exclusivity to cover temporal duration as well, promises to develop these alternatives in detail.

Compulsory Licensing and a Statutory Fee

An alternate approach to the copyright problem involves legislative or regulatory specification of a fixed fee for cable use of imported signals. Under this plan, the program owners' copyright would be extended to cover cable pickup, but would be subject to a requirement for compulsory licensing with respect to

a specified number of distant signals.

The argument for this approach is simple: cable revenues from subscribers would be more than ample to fully compensate the owners of imported programs for any revenue lost through importation. Current regulations and exclusivity practices frustrate such a mutually beneficial arrangement; therefore, regulation can serve both to accommodate the conflicting private interests and make cable available to an interested public.

This reasoning lies behind a plan which the F.C.C. presented for public discussion a year ago. In the F.C.C.'s plan, copyright owners would receive, as a group, fees from cable importers of distant signals; the fee rate, calculated as a percentage of the importers' gross revenues, would be designed to approximate aggregate copyright losses.[19]

As compared with the alternative of restrictions on exclusivity, the statutory licensing plan may be objectionably arbitrary. There is no reason why cable systems, more than broadcasters, should have the benefit of fixed statutory copyright fees. If fees are to be limited in any way, the rationale must be that exclusivity disadvantages the small customer. But

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19. In addition, the F.C.C.'s plan proposed compensating local stations for lost audience by providing for substitution of commercials broadcast by those local stations for those coming over the imported distant signal. The Chazen and Ross article, supra, suggested using such substitution to compensate copyright owners. At the F.C.C. panel discussion of cable television in March, 1971, the weight of technical commentary was against the feasibility of commercial substitution, and comments from Commissioners indicated that the plan is no longer a serious prospect.

A final feature of the Commission's proposal was a payment of 5 per cent of subscriber revenues by cable operators, for the benefit of non-commercial TV.

this argument applies as well to UHF stations as to cable systems, and suggests that modification of exclusivity would be the more even-handed answer.

If, however, restrictions on exclusivity are technically or politically infeasible, then compulsory licensing has the advantage described earlier: it makes the immediate parties to the controversy (cable and copyright interests) better off than at present, and removes a barrier to public demand for the cable. It does, of course, threaten the market power of large broadcasters; but that is precisely what a pro-competitive policy would command.

Full Copyright Liability

An explicit decision for full copyright liability would, in effect, continue the current situation; since the F.C.C.'s interim rules on retransmission consent, there has been little regulatory barrier to cable importation of programs arriving over distant signals where permission has been obtained from the copyright owner. The most likely outcome of such a decision is that the present impasse would continue; copyright owners would, as the author has been told informally, find it impossible to break on an individual basis with the practice of exclusivity.

Summary and Future Prospects

At present, growth of cable seems to hinge on the modification of copyright exclusivity, either directly or through the roundabout device of compulsory licensing. If, however, cable growth proceeded on some other basis copyright owners might well eventually find cable sufficiently alluring to justify risking broadcasters' good will.

For example, if the government subsidized cable for 75% of the nation's homes, then copyright owners could afford to ignore broadcasters altogether. But any such prospect seems unlikely, and the future of cable in all probability depends upon a resolution of the copyright impasse.